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The Information

THE TAKEAWAY

The Truth About Uber's Otto Deal

By Jessica E. Lessin Dec. 02, 2016 7:01 AM PST

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I was recently calling sources about the biggest tech M&A deals of 2016 and came across an interesting fact. Uber's acquisition of Otto (described **here** by the company) isn't quite as it appears.

While it's been widely covered as a deal in which Uber paid $680 million in equity for the self-driving trucking company, the reality is more complicated. Unlike typical deals, Uber acquired Otto shares without paying upfront, apart from some nominal cash to close the deal. Instead, the company struck a more unusual arrangement with two parts.

THE TAKEAWAY

Uber put an unusual incentive plan in place when it acquired Otto this summer, showing how private tech deals aren't always as they appear.

The first is that Otto's shareholders—comprised of its co-founders and employees—were promised up to 1% of Uber's equity over time, depending on how many self-driving Uber cars hit the road and other technical milestones. (This is where the reported $680 million number came from, based on Uber's valuation at the time.)

It's a pretty good deal for Uber, which could end up paying out much less in stock if the milestones are not met. That means Uber is hedged against Otto's team, now responsible for Uber's entire self-driving car project, not living up to its mission. It's also highly unusual. Most deals give sellers some money or stock upfront, even if much of the payment price is dependent on how their business performs after the sale.

The second element of the deal, which has been previously reported, gives Otto's former owners 20% of the profits generated from the Otto trucking service. That's the service that just delivered 50,000 cans of Budweiser across Colorado. This part sweetened the deal for Otto shareholders, letting them hang on to some of the profits from the technology they are turning over.

It may seem strange for Otto shareholders to turn over the company for nothing upfront, but Otto wasn't a typical startup. For one, its founders were already very wealthy from their time at Google and other projects. They self-funded Otto with some $6 million of their own money. About half came from founder Anthony Levandowski, according to someone familiar with the company's formation. And with no outside shareholders, there were no VCs to feed.

Levandowski is a self-driving car pioneer who joined Google in 2007 and sold it some IP that sparked its self-driving car project. As that project lingered in development, he left Google in 2016 to start Otto and commercialize self-driving technology faster. The company was bought just months after its launch.

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The team has always been more interested in commercializing self-driving technology at a big company rather than going at the capital-intensive business alone. So joining Uber made a lot of sense.

The fine print of the Uber-Otto alliance once **again confirms** that, when it comes to private tech M&A, the headline price can be misleading. I'm sure there are many self-driving car startups benchmarking their valuations off the Uber-Otto deal. They should know the whole story.

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The structure of the deal also provides some hints about what Uber saw with Otto. Like so many tech deals these days, it is really about the team more than the current technology. Self-driving car tech is moving quickly so Otto's technology today isn't worth as much to Uber as what a veteran who was for years at the center of Google's efforts can develop tomorrow.

Just as Marc Benioff and Salesforce bought Quip for $750 million in cash and stock to work with CEO Bret Taylor and Walmart bought Jet.com for more than $3 billion in cash to nab CEO Marc Lore, companies are paying hundreds of millions and billions for founders. Uber wanted what was in Levandowski's brain and devised a clever way to pay for it.

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Hendrik Laubscher
Development Strategist, PriceCheck

3 months ago

Fascinating insight into a potential model for other self driving car startups being acquired. Is the 1% in future uber shares a set amount as a potential 110x return being hedged against performance is risky to state it mildly.

Like · Leigh Ann Arthur liked this.

Chad Grills
Founder, The Mission

3 months ago

"Uber wanted what was in Levandowski's brain and devised a clever way to pay for it."

Well said. This is a trend that will ramp up. Big companies know they desperately need real entrepreneurs or artists in residence. But paying an EIR or AIR the amount of money their unique expertise is worth is tricky to justify to the rest of the company and shareholders.

I suspect that most Founder CEO's know how important the issue of internal employee compensation can be for a healthy culture. It's really hard to justify paying certain employees 10x more than others. This seems to be an excellent way to get around that challenge. It might be ego shattering for previous Uber employees to face the fact that the newest additions to the team from Otto are making 10x times more, with a piece of the upside, but it seems like a solid way to align incentizes. I'm curious to see how this plays out.

It seems like big companies are going to keep finding clever ways to prevent mutiny inside their cultures, while also paying astronomical sums to rent the brains of certain founders. Right now, this trend is prevalent for "technical" founders and companies like Otto. But I expect it to start ramping up amongst creatives and artists. Soon, we'll see AIR as a common title inside tech companies. The recent CNN acquisition of Casey Neistat's Beme is the beginning of that trend (which will accelerate as budgets for original content and media go up at places like Amazon, HBO, Netflix, etc...).

Kudos for finding and telling the story behind the story.

Like · Taylor Davidson and Stewart Mc Dowell liked this.

John Danner
CEO, Zeal Learning

3 months ago

Great piece. The insight that this was only possible because of lack of venture seems right on to me. The founder is willing to bet big that he can make uber a much more valuable company, love it.

Like

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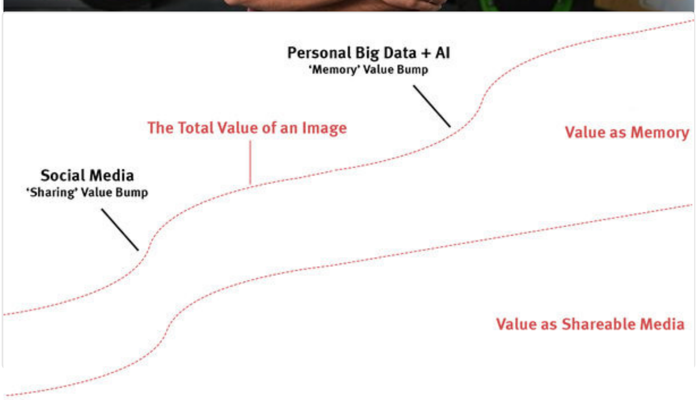

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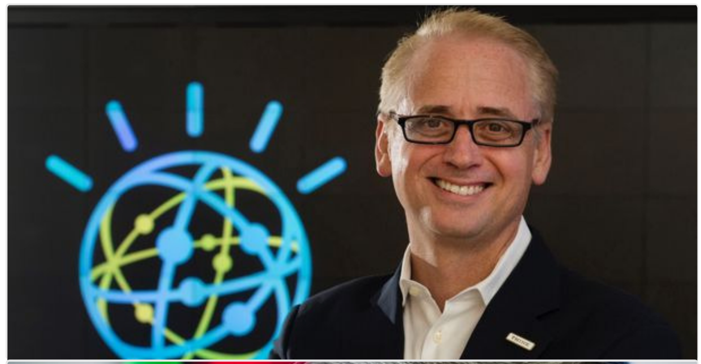

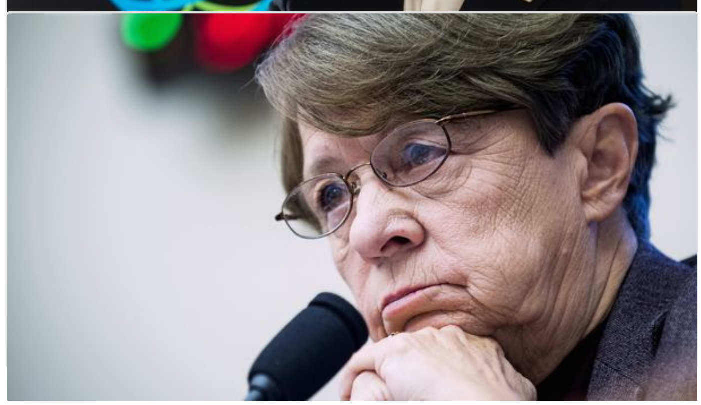

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